



**U.S. DEPARTMENT OF JUSTICE
Antitrust Division**

**INTELLECTUAL PROPERTY AND THE ANTITRUST LAWS: PROTECTING
INNOVATORS AND INNOVATION**

Address by

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I am very pleased to have the opportunity to appear here before the annual winter meeting of the Licensing Executives Society. This organization serves the interests of the intellectual property community and the nation by emphasizing the importance of licensing arrangements to our economy and by sponsoring programs such as this conference to promote the exchange of information about efficient licensing practices. As a member of the Clinton Administration, and as a proud citizen, I applaud your efforts.

The generally pro-competitive nature of licensing arrangements is a core principle of the proposed Department of Justice Guidelines for the Licensing and Acquisition of Intellectual Property. Licensing promotes the diffusion of knowledge and enhances the utilization of intellectual property. I use the term licensing, as it is used in the proposed Guidelines, in a broad sense to include all forms of joint ventures or other partnering activities in addition to arms-length transactions in which the exchange of knowledge or the use of knowledge assets is an important part of the deal. In today's economy, technology partnerships are essential to remain globally competitive and to market the products that knowledge assets help to create. As the world continues to become a more competitive place, and as firms scattered across the globe develop their own technological advantages,

licensing plays an increasingly vital role to ensure that America's industries remain at the technological frontier. The Licensing Executives Society deserves recognition for the important job it has done in promoting these essential technology partnering activities.

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The United States continues to lead the world in the creation and use of new technology. Last September, the Geneva-based World Economic Forum identified the United States as the world's most competitive economy. Such a comparison may seem arbitrary -- a "most likely to succeed" opinion poll on an international scale. But if you examine the report, I expect you will be as impressed as I by the number and scope of economic indicators they employed. It is not surprising that a significant contributor to the competitiveness scoreboard is a nation's R&D infrastructure. In the Science and Technology category, the World Economic Forum included 42 criteria. Among them, the United States ranked first compared to all nations in expenditures on total R&D, business R&D, and basic research. We ranked first in the total number of patents and fifth in the rate of patents granted per capita to domestic residents. The U.S. has the largest number of scientists and engineers, and the largest number of R&D personnel in industry. We ranked third among all nations in the adequacy of protection for intellectual

property, close behind only Austria and Switzerland. The United States was awarded an "8" in this category, on a scale of 1 to 10, based on survey responses. China, much in the news lately, earned a "3" in this category, surpassing only Russia in the adequacy of protection for intellectual property.

There is a high correlation between the protection that a nation provides for owners of intellectual property and its success in creating economic prosperity. Of the top ten nations in the category of adequacy of protection for intellectual property, five are among the top ten in gross domestic product per capita, and none rank below number 17 in per capita GDP. Japan is a notable exception to this correspondence, with a very high level economic production, yet weak protection for intellectual property. However, even Japan has made progress lately in connection with the recent GATT negotiations toward increasing protection for owners of intellectual property, both domestic and foreign.

To some extent, the correlation between the strength of IP protection and economic prosperity arises because richer countries have more to lose from weak intellectual property rights. But this is much too simplistic an answer. The reality is that even the technology have-nots must protect intellectual property if they are going to attract international investment and compete and prosper in the global economy.

I was also curious about the findings of the World Economic Forum on the relative efficiency of government. The U.S. ranked a rather dismal 25th in "effectively adapting its policies to new economic realities". We're trying to do something about that. On a brighter note, the U.S. was second in the survey response to "whether the antitrust laws prevent unfair competition in your country," lagging behind only Germany. I take pleasure in pointing out a high, if not perfect, correlation between a country's survey response ranking on the effectiveness of its antitrust laws and the country's ranking in per capita gross national product.

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If it is so obvious that economic progress and intellectual property protection go hand-in-hand, then what role is there for antitrust in commerce affecting intellectual property?

In the past, there has been a tension between the need to protect the rights of intellectual property owners and the need to protect consumers. But modern thinking has long abandoned the concept that antitrust and intellectual property are at loggerheads. As the court observed in *Atari Games Corp. v. Nintendo of America, Inc.*,¹ "the aims and objectives of patent and antitrust laws may seem, at

¹ 897 F.2d 1572, 1576 (Fed. Cir. 1990).

first glance, wholly at odds. However, the two bodies of law are actually complementary, as both are aimed at encouraging innovation, industry and competition.” Without intellectual property rights, the incentive to invest and innovate would be greatly diminished. That result would be contrary to the very purpose of the antitrust laws, which is to promote the well-being of consumers by spurring efficiency, innovation, and investment.

There is much evidence to support the view that markets in which competition is permitted and encouraged to flourish are also markets that are the most innovative and progressive. You may have heard me or others in the Antitrust Division cite Michael Porter's comprehensive study, *The Competitive Advantage of Nations*, in which he found that a highly competitive domestic market is a likely driving force for achieving international economic advantage. Other studies of the determinants of economic advantage have reached similar conclusions. For example, David Mowery and Nathan Rosenberg studied the relationship between research and development policy and economic growth in a historical context.² They concluded that a lax antitrust policy was part of the explanation for England's poor record of manufacturing productivity growth in the

² David C. Mowery and Nathan Rosenberg, *Technology and the Pursuit of Economic Growth*, Cambridge University Press (1989).

first half of this century. Trade agreements allowed weak industries to survive and postponed the inevitable restructuring that was necessary to compete in global markets.

Our nation is committed to antitrust laws protecting competitive markets, because competition rewards those who create new, better, or cheaper goods and services. In this way, competition inspires imagination and invention. In contrast, monopoly that is not the consequence of inventive activity rewards established institutions and is often opposed to change. By protecting competition and innovation, our antitrust laws contribute to the ability of our nation to create economic value and to compete in a global economy.

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I've said enough about the state of the world. Now I'll turn to the state of the Department of Justice Intellectual Property Guidelines. The Division reconsidered its Intellectual Property Guidelines as part of a more general effort to revise its 1988 International Guidelines. It was also an opportunity to re-examine antitrust policy in a critical area of the economy. It was not our intention to produce IP Guidelines that are dramatically different from what had been issued in the past, and it is no accident that the new proposed Guidelines espouse the same basic principles. Central among these principles is, as I have already mentioned, the

generally procompetitive nature of licensing. Another key principle, which should be common sense to anyone who has worked in or around research and development, is that intellectual property does not necessarily convey market power in the antitrust sense. Although a patent, copyright or trade secret may provide protection for a product that is significant enough to be considered a separate antitrust market, often there are many alternatives to the intellectual property and the IP protection is sufficiently limited to prevent the exercise of significant market power.

The third key principle in the IP Guidelines is that the Agencies should apply the same general approach under the antitrust laws to conduct involving intellectual property that they apply to conduct involving any other form of tangible or intangible property. This is not to say that intellectual property is the same in all respects as other forms of property, or that all forms of intellectual property, such as patents and trade secrets, are the same. However, antitrust policy can be applied flexibly to account for these differences, and there is no need either to carve out antitrust exemptions for intellectual property, or to treat intellectual property more harshly under the antitrust laws.

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We received 34 comments on the Guidelines. Most of them, including the

comments we received from this Society, are thoughtful and constructive.

Working with the Federal Trade Commission, who we hope will be co-sponsors of the Guidelines, we intend to respond to them to the best of our ability, consistent with maintaining the broad principles of the Guidelines and not undermining our capacity to carry out our antitrust enforcement mission.

A number of the commentators want the Guidelines to be more specific. It is easy to understand and sympathize with the plight of the attorney who must counsel his client on the arcane teachings of the antitrust laws and the complex ways in which they interact with the intellectual property laws. It is no surprise that there is a plea for a simple prescription. But the Guidelines will not be as specific as many say they would like them. Indeed, I sincerely doubt that the business community would want us to deliver the specific guidelines that some have requested.

The Intellectual Property Guidelines are guidelines, they are not regulations. Although clarity is a goal of the Guidelines, the price of clarity is too high if it means adopting wooden per se rules of illegal conduct, or if it means adopting blanket statements of permitted conduct when such behavior can be anticompetitive in some contexts.

It is difficult to satisfy a desire for more specific direction in the Intellectual

Property Guidelines without advancing the equivalent of bright line rules, such as the Department of Justice "nine no-no's" of patent licensing in the 1970s. A wish for clarity could translate into a nightmare of arbitrary policies that are too strict for some circumstances while overlooking potential abuses in others.

Some commentators, including this Society, have expressed concerns with the use of technology and innovation markets in the Guidelines. The general concerns are that technology and innovation markets may be difficult to define, that these difficulties insert additional uncertainties into antitrust analysis, and that they are unnecessary because relevant competitive effects may be captured in downstream product markets.

I agree that in the final analysis the competitive effects of an arrangement, if any, will appear in one or more product markets for goods and services that consumers buy. However, there are circumstances where technology or innovation markets provide the right tools to identify and analyze these effects.

As an example, how would you treat the following situation? Suppose there are many ways to make a particular vitamin. The market for the sale of the vitamin is highly concentrated, perhaps because it involves very large marketing expenses. But many firms compete to supply the downstream market with the active ingredient for the vitamin. They do so with different technologies, some of which

may be patented and licensed from others.

Now suppose two of the firms that make processes for the active ingredient merge. In my example, the merger may not present a problem for competition if there are many ways to make the necessary active ingredient. But if you focused on the downstream product, you might conclude, erroneously, that the merger is a problem because the downstream product market is highly concentrated.

Alternatively, there may be a large number of firms that market vitamins, but all of these firms may license the technology for the active ingredient from one of two firms, and not all of the vitamin marketers license the active ingredient from the same firm. A merger of the two active ingredient suppliers could have significant effects on the price of vitamins, even if the downstream market has a competitive structure. How should we avoid mistakes that might occur from too narrow a focus on product markets if the Department is not permitted to analyze competition in technology markets?

The revised Guidelines will be more explicit about when technology markets are useful and how market shares could be estimated in such a market. However, eliminating technology markets altogether would risk losing a tool that is needed to analyze properly the competitive effects of some transactions.

Similar concerns have been expressed with regard to Innovation markets.

Let me first say that under the National Cooperative Research and Production Act, the Department is required to analyze the competitive effects of joint ventures that register under the Act in markets that include relevant research and development markets. This was recognized in the 1988 Guidelines. The 1988 Guidelines included a case study of a research and development joint venture (Case 6), and states that "The Department would begin its analysis by defining the relevant R&D market and identifying firms that compete in that market."

Putting the statutory requirement for research and development markets aside, one can ask what is gained from the use of innovation markets that cannot be accomplished by focusing on downstream product markets. For an answer, consider a research joint venture to produce, say, a new type of plastic that is easily biodegradable. There might be a concern that the joint venture will slow, rather than hasten, the development of this product. This might occur perhaps because the adoption of the new plastic will create opportunities for new winners and losers in the plastics industry, which would be a threat if the industry had enjoyed stable market shares, or because development of the new plastic might be a stimulus for new environmental regulations that the industry would like to avoid. The product to be developed by the joint venture does not yet exist and there may be nothing comparable, so product market shares are not useful to an analysis of the

competitive effects of the joint venture. To analyze this venture, you either have to consider the joint venture participants as potential entrants into a non-existent product market, or you must address the competitive effects in a relevant market that would include innovation of biodegradable plastics. The latter focuses on the correct question, which is whether the joint venture would control a significant fraction of the R&D that would be likely to be applied to the development of this type of a product, and, if so, whether the joint venture participants would have an incentive to reduce total industry R&D effort. In addition, if the joint venture might lessen R&D, the analysis should address whether there are efficiency benefits that might outweigh the possible anticompetitive effects.

It should be clear that an analysis of innovation markets is appropriate only in some circumstances. In many industries, almost anyone anywhere can engage in R&D. It is essentially impossible to monopolize R&D in such a market. To keep the issue of innovation markets in perspective, you should note that the last time the Department challenged an R&D joint venture was in 1975.

The revised IP Guidelines are likely to state that the Agencies will delineate and analyze only goods markets when the competitive effects of a licensing arrangement can be adequately addressed within the relevant markets for the goods affected by the arrangements. That is, the Agencies will not use innovation

markets or technology markets when they are not necessary for an adequate competitive analysis. However, as in the examples I have just given, there are circumstances where innovation or technology markets are necessary for an adequate analysis of competitive effects.

Let me briefly address three other comments. Some commentators have urged the Department to reconsider the need for using any per se analysis, and instead propose a rule of reason treatment for all licensing arrangements. In fact, I expect that our approach will yield rule of reason treatment for any licensing arrangement that involves a legitimate transfer of technology. It is also consistent with the development of the law with respect to conduct that could be subject to per se rules. A good example is the Broadcast Music case,³ in which the Supreme Court cautioned against an "overly simplistic and overly broad" application of per se rules when the Court determined that an agreement among 40,000 authors and composers to set standard royalties for nonexclusive blanket licenses was not a violation of the antitrust laws. The Court reasoned that the agreement was an efficient way to overcome significant transaction costs and that the efficiencies created, in effect, a new product that would not otherwise exist. In other words, our approach accords with the Court's increasing reliance on the rule of reason.

³ Broadcast Music, Inc. v. CBS, 441 U.S. 1 (1979).

The revised Guidelines also are likely to state more clearly that a nonexclusive license is rarely a competition problem, absent restraints on the competitive conduct of the licensor or the licensee. However, I think you can understand that the mere label of a nonexclusive license cannot be sufficient to exempt the transaction from antitrust scrutiny.

Some commentators have requested that the protection of the proposed safety zone be permanent, whether or not the licensed product remains within the confines of the 20 percent market share that defines the limit of the safety zone. The reason for this request is understandable. Parties to a licensing arrangement are concerned about antitrust liability for the life of the contract and do not want success to be punished. However, the safety zone is not an antitrust exemption for transactions that fall within the safety zone at any point in time, nor should it be. As an example, I do not believe it is in the best interest of the nation for the Antitrust Division to be prohibited from reviewing the licensing activities of Microsoft's Windows operating system product because, in 1984, the market share of Microsoft Windows in the relevant antitrust markets was less than 20 percent.

Intellectual property is, and will continue to be, the engine of economic growth for our economy. America needs strong intellectual property rights to protect the innovators that have helped to build today's economy, and to encourage

the innovators who will build the foundation of tomorrow's economy. Consumers, as well as the owners of intellectual property, are the beneficiaries of investment in our intellectual property infrastructure. At the same time, we must ensure that intellectual property rights are used as intended to promote and reward innovators, and that they are not used to discourage innovation by others through means that extend beyond the proper limits of these rights. Responsible antitrust enforcement creates conditions that allow entrepreneurial initiative to flourish by assuring that innovators, having crossed the threshold of discovery, are not stopped in their tracks by a wall of closed and anticompetitive markets. I assure you that the Antitrust Division will continue to provide vigilant and responsible enforcement of the antitrust laws as they apply in intellectual property arrangements and in every other sector of our economy.